Report

of the

Examination of

Medina Mutual Insurance Company

Marshall, Wisconsin

As of December 31, 2004

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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May 13, 2005

Honorable Jorge Gomez
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
Madison, Wisconsin 53702

Commissioner:

In accordance with your instructions, an examination has been performed as of December 31, 2004, of the affairs and financial condition of:

MEDINA MUTUAL INSURANCE COMPANY
Marshall, WI

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The previous examination of Medina Mutual Insurance Company (hereinafter MMIC or the company) was made in 2000 as of December 31, 1999. The current examination covered the intervening time period ending December 31, 2004, and included a review of such subsequent transactions deemed essential to complete this examination.

The “Summary of Examination Results” contains elaboration on all areas of the company's operations. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company was organized as a town mutual insurance company on June 12, 1875, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Farmers’ Mutual Protective Fire Insurance Company. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

During the period under examination, there were no amendments to the articles of incorporation and no amendments to the bylaws.

The company is currently licensed to write property, including windstorm and hail, and nonproperty insurance. The company is currently licensed to write business in the following counties:

Columbia	Crawford
Dane	Dodge
Grant	Green
Iowa	Jefferson
Lafayette	Richland
Rock	Sauk
Walworth	

A review was made of the policy and application forms currently used by the company. The company issues approved policies with or without endorsements for terms of one and three years with premiums payable on the advance premium basis. The company also charges installment fees of $10.00 per quarterly installment and $5.00 per semiannual installment for policies that are billed in installments other than annual.

Business of the company is acquired through 62 agents, 3 of whom are directors of the company. Agents presently receive a 15% commission on all lines of business written.

Agents do not have authority to adjust losses. Losses are adjusted by an appointed adjusting committee. An outside adjuster is used when complex issues arise or if major storms occur that exceed the capabilities of the adjusting committee to investigate claims in a timely manner. Director-adjusters receive $40.00 for each loss adjusted plus $0.40 per mile for travel allowance. An additional $15.00 per hour is paid to director-adjusters for claims that take longer than four hours to adjust.

Policyholders may participate in the management and control of the company by attending and voting at all annual or special meetings of the members. No member may vote by proxy. The annual meeting of the company for the election of directors and special meetings of the company are held in accordance with its articles of incorporation.

Board of Directors

The board of directors consists of seven members divided into three classes. One class is elected at each annual meeting for a term of three years. Vacancies on the board may be filled by the directors for the interim to the next annual meeting when a director shall be chosen for the unexpired term.

The current board of directors consists of the following policyholders of the company:

Name	Principal Occupation	Residence	Expiry
Wesley Dorshorst	Farmer and snow plow operator for the City of Sun Prairie	Deerfield, Wisconsin	2005
Russell Haupt	State employee for DILHR-PECFA	Arlington, Wisconsin	2005
Robert Michel*	Retired seed salesperson	Cambridge, Wisconsin	2005
Duane Hinchley	Farmer	Cambridge, Wisconsin	2006
Darrell Langer*	Part-time farmer and president and manager of Medina Mutual Insurance Company	Marshall, Wisconsin	2006
John Bornitzke*	Farmer	Marshall, Wisconsin	2007
Elmore Schulenberg	Retired postal employee	Sun Prairie, Wisconsin	2007

Directors who are also agents are identified with an asterisk (*).

Members of the board currently receive $75.00 for each meeting attended and $0.40 per mile for travel expenses.

Officers

Officers are elected by the board of directors from among its members and hold office for one year or until their successors are duly elected and qualified. Officers serving at the present time are as follows:

Name	Office	2004 Salary
Darrell Langer	President, Manager	$21,000*
Robert Michel	Vice-President	0*
Wesley Dorshorst	Secretary	2,500
John Bornitzke	Treasurer	4,000*

* President, Vice President and Treasurer also receive commissions as agents. For 2004 Mr. Langer received $55,243 in commissions, Mr. Michel received $8,603 in commissions and Mr. Bornitzke received $8,408 in commissions.

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committee at the time of the examination is listed below:

Adjusting Committee
Darrell Langer, Chair
John Bornitzke
Wesley Dorshorst

Growth of Company

The growth of the company since the previous examination as compiled from its filed annual statements was as follows:

Year	Net Premiums Earned	Policies In Force	Net Income	Admitted Assets	Policyholders' Surplus
2004	$1,104,695	2,377	$ 197,480	$2,625,583	$1,348,075
2003	932,969	2,078	272,438	2,027,295	1,064,357
2002	590,130	1,752	64,478	1,538,229	785,040
2001	414,654	1,287	(194,490)	1,383,624	826,403
2000	346,854	1,072	75,893	1,494,643	1,091,335
1999	313,609	995	(193,089)	1,529,956	1,037,221

The ratios of gross and net premiums written to surplus as regards policyholders since the previous examination were as follows:

Year	Gross Premiums Written	Net Premiums Written	Ending Surplus	Writings Ratios Net	Writings Ratios Gross
2004	$1,840,095	$1,274,736	$1,348,075	95%	137%
2003	1,528,015	1,070,743	1,064,357	101	144
2002	1,204,247	751,768	785,040	96	153
2001	843,494	528,703	826,403	64	102
2000	675,490	371,296	1,091,335	34	62
1999	605,856	352,416	1,037,221	34	58

For the same period, the company's operating ratios were as follows:

Year	Net Losses and LAE Incurred	Other Underwriting Expenses Incurred	Net Earned Premiums	Loss Ratio	Expense Ratio	Com-posite Ratio
2004	$385,832	$437,737	$1,104,695	35%	34%	69%
2003	312,945	368,012	932,969	34	34	68
2002	253,074	297,034	590,130	43	40	83
2001	426,748	236,463	414,654	103	45	148
2000	151,817	190,943	346,854	44	51	96
1999	385,576	166,065	313,609	123	47	170

Business written has increased significantly over the past five years beginning in 2000, which was partially attributable to rate increases and inflation in housing prices, but mostly due to aggressive marketing through the increase of their agency force. Gross premium written has increased by 204% and policies in force increased by 139% over this period. It was noted that business growth has been spread out over the company's territory, reducing concern about concentration of risk.

Over the past three years, the company's growth coupled with favorable weather conditions produced very good underwriting results, which is reflected in the company reporting an average net income of $178,132 and an increase to surplus of 63%. In the last three years, gross premiums written increased 118% and net premiums earned increased 166%, which resulted in the company's expense ratio decreasing over that same period, due to expenses increasing only 85% during that period. In April and June 1999 the company suffered large wind and hail storms and settled claims that were not fully adjusted from wind storms that occurred in November 1998. As a result of these events the company reported a net loss ratio of 123% and a net loss of $194,490 at year-end 1999. Claims from these storms were not fully settled until 2001, which contributed to the 103% net loss ratio reported that year.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty contained a proper insolvency clause and complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

Reinsurer:	Wisconsin Reinsurance Corporation
Effective date:	January 1, 2004, continuous
Termination provisions:	By either party, on any January 1, with 90 days' advanced written notice

The coverages provided under this treaty are summarized as follows:

1.	Type of contract:	Excess of Loss (Class A)
	Lines reinsured:	Liability (nonproperty)
	Company's retention:	$5,000 for each and every loss occurrence up to policy limits
	Coverage:	100% in excess of retention including loss adjusting expense. Subject to policy limits of $1,000,000 for bodily injury and property damage, and $5,000 per person and $25,000 per accident for medical payments
	Reinsurance premium:	55% of gross liability premiums charged for each policy issued, which equals the liability reinsurance rates
2.	Type of contract:	First Surplus (Class B)
	Lines reinsured:	All property business
	Company's retention:	$400,000 of each risk ceded pro rata. If net retention for a risk is $400,000 or less the company may cede 50% pro rata
	Coverage:	Pro rata portion of each loss and LAE up to $800,000 above retention
	Reinsurance premium:	Pro rata portion of premium and fees on each risk ceded
	Ceding commission:	15% of the premiums paid to the reinsurer
	Profit commission:	15% of the net profit calculated as follows: a) Premiums earned for the period; less b) Ceding commission allowed the company on premiums earned for the period; less c) 10% of premiums earned for the period to cover incurred expenses; less

d) Losses and LAE incurred for the period; less the reinsurer's net loss, if any, from the preceding period.

3.	Type of contract:	Excess of Loss (Class C-1)
	Lines reinsured:	All property business written
	Company's retention:	$30,000 for each and every risk from one loss occurrence
	Annual aggregate deductible:	First $30,000 of paid losses
	Coverage:	$70,000 each and every risk and loss occurrence, including loss adjusting expense, above retention
	Reinsurance premium:	Rate based on net premium written and losses incurred for immediate preceding four years. Minimum rate of 6% and maximum rate of 21.5% of current net premium written. The 2004 annual rate is 7.5%. Minimum premium of $77,500
4.	Type of contract:	Second Excess of Loss (Class C-2)
	Lines reinsured:	All property business written
	Company's retention:	$100,000 each and every risk from one loss occurrence
	Coverage:	$300,000 each and every risk and loss occurrence, including loss adjusting expense, above retention
	Reinsurance premium:	3.5% of net premiums written for business covered subject to minimum premium of $36,000 and deposit premium of $45,300
5.	Type of contract:	First Aggregate Stop Loss (Class D/E)
	Lines reinsured:	All business written
	Company's retention:	Losses in aggregate equal to 67.5% of the net premiums written and a minimum amount of retention of $768,000 in the aggregate for the year
	Coverage:	100% of aggregate losses, including loss adjustment expenses, in the annual period that exceed the retention
	Reinsurance premium:	Rate of losses incurred divided by net premiums written for last eight years losses incurred times 125%, applied to net premiums written with a minimum rate of 7.5% and maximum of 25%. The 2004 annual rate is 7.5%. Minimum premium of $85,000

III. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2004, annual statement. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Policyholders' Surplus."

Medina Mutual Insurance Company
Statement of Assets and Liabilities
As of December 31, 2004

Assets	**Ledger**	**Nonledger**	**Not Admitted**	**Net Admitted**
Cash deposited in checking account	$ 104,771	$	$	$ 104,771
Cash deposited at interest	1,457,049			1,457,049
Stocks and mutual fund investments	536,608			536,608
Real estate	67,323			67,323
Other invested assets	103,944			103,944
Premiums, agents' balances and installments:				
In course of collection	72,099		340	71,759
Deferred and not yet due	267,868			267,868
Investment income accrued		8,255		8,255
Electronic data processing equipment	8,006			8,006
Furniture and fixtures	1,735		1,735	0
Totals	$2,619,403	$8,255	$2,075	$2,625,583

Liabilities and Surplus

Net unpaid losses	$ 113,500
Unpaid loss adjustment expenses	700
Commissions payable	43,700
Fire department dues payable	2,170
Federal income taxes payable	112,334
Unearned premiums	874,693
Reinsurance payable	70,656
Amounts withheld for the account of others	5,234
Payroll taxes payable (employer's portion)	1,090
Other liabilities:	
Expense-related:	
Accounts payable	1,221
Accrued property tax	3,691
Nonexpense-related:	
Premiums received in advance	48,519
Total Liabilities	1,277,508
Policyholders' surplus	1,348,075
Total Liabilities and Surplus	$2,625,583

Medina Mutual Insurance Company
Statement of Operations
For the Year 2004

Net premiums and assessments earned		$1,104,695
Deduct:		
Net losses incurred	$361,668	
Net loss adjustment expenses incurred	24,164	
Other underwriting expenses incurred	437,737	
Total losses and expenses incurred		823,569
Net underwriting gain (loss)		281,126
Net investment income:		
Net investment income earned		30,962
Other income (expense):		
Other Income		2,592
Net income (loss) before federal income taxes		314,680
Federal income taxes incurred		117,200
Net Income (Loss)		$ 197,480

Medina Mutual Insurance Company
Reconciliation and Analysis of Surplus as Regards Policyholders
For the Five-Year Period Ending December 31, 2004

The following schedule is a reconciliation of surplus as regards policyholders during the period under examination as reported by the company in its filed annual statements:

	2004	2003	2002	2001	2000
Surplus, beginning of year	$1,064,357	$ 785,040	$826,403	$1,091,335	$1,037,221
Net income	197,480	272,438	64,478	(194,490)	75,893
Net unrealized capital gains or (losses)	35,438	48,981	(99,244)	(72,012)	(20,912)
Change in nonadmitted assets	50,800	(42,102)	(6,597)	1,570	(867)
Surplus, end of year	$1,348,075	$1,064,357	$785,040	$ 826,403	$1,091,335

Reconciliation of Policyholders' Surplus

A reconciliation of the policyholders' surplus as reported by the company in its filed annual statement and as determined by the examination is detailed in the following schedule:

Policyholders' surplus per December 31, 2004, annual statement			$1,348,075
Item	**Increase**	**Decrease**	
Premiums in course of collection	$	$19,932	
Net unpaid losses		19,602	
Total	$ 0	$39,534	
Decrease to surplus per examination			(39,534)
Policyholders' Surplus per Examination			$1,308,541

Examination Reclassifications

	Debit	Credit
Premiums received in advance	$21,017	$ 0
Premiums deferred and not yet due		21,017
Total reclassifications	$21,017	$21,017

IV. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

Comments and recommendations contained in the last examination report and the action taken on them by the company are as follows:

1. Conflict of Interest—It is recommended that each director of the company sign a conflict of interest statement annually.

   Action—Compliance

2. Underwriting—It is recommended that the company establish a formal inspection procedure for new and renewal business.

   Action—Compliance

3. Underwriting—It is again recommended that the company include "inspection reports" in its policy files.

   Action—Compliance

4. Underwriting—It is recommended that the company reconcile reinsurance records to current information contained in policy files.

   Action—Compliance

5. EDP Environment—It is recommended that the company store daily backed-up data in a fireproof safe on-site. The company should also establish a procedure in which its computer system is backed up at least weekly and the backed-up data is kept in a safe place separate from the location where the computer is kept. The data back-up procedures should be added to the company's disaster recovery plan.

   Action—Compliance

6. Investments—It is recommended that the company adopt a written plan for engagement in investment practices in accordance with s. Ins 6.20 (6) (h), Wis. Adm. Code.

   Action—Compliance

7. Investments—It is recommended that the company make no additional Type 2 investments until the company meets the required amount of Type 1 investments, pursuant to s. Ins 6.20 (6) (c), Wis. Adm. Code.

   Action—Noncompliance, see comments in the summary of current examination results under the section titled "Investment Rule Compliance."

8. Investments—It is recommended that investments in mutual funds shall have a minimum rating of four-stars from Morningstar Mutual Funds, Inc., pursuant to s. Ins 6.20 (6) (d) 3. c., Wis. Adm. Code.

   Action—Compliance

Current Examination Results

Corporate Records

The minutes of the annual meetings of policyholders and meetings of the board of directors and committees thereof were reviewed for the period under examination and also for the subsequent period.

Biographical data relating to company officers and directors have been reported in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

The company has executed formal written agreements with its agents. The contracts include language indicating the agent will represent the company's interests "in good faith."

Conflict of Interest

In accordance with a directive of the Commissioner of Insurance, each company is required to establish a procedure for the disclosure to its board of directors of any material interest or affiliation on the part of its officers, directors, or key employees which conflicts or is likely to conflict with the official duties of such person. A part of this procedure is the annual completion of a conflict of interest questionnaire by the appropriate persons. The company has adopted such a procedure for disclosing potential conflicts of interest. Conflict of interest questionnaires were reviewed for the period under examination with no apparent conflicts being noted.

Fidelity Bond and Other Insurance

The company is afforded coverage under the terms of the following bonds or contracts and has complied with s. Ins 13.05 (6), Wis. Adm. Code, which sets forth the minimum requirements for fidelity bond coverage:

Type of Coverage	Coverage Limits
Fidelity bond:	
Manager and office employees	$ 125,000
Worker's compensation:	
Employee injury	Statutory
Employee liability:	
Bodily injury (per accident)	100,000
Bodily injury (per employee for disease)	500,000
Policy limit	500,000
Property coverage:	
Building	300,000
Personal property	200,000
Personal liability:	
Liability (per occurrence)	1,000,000
Medical expenses (per occurrence)	25,000
Medical expenses (per person)	1,000
Office rental to others	1,000,000
Professional liability:	
Per claim limit	1,000,000
Aggregate limit	1,000,000
Deductible	5,000
Directors and officers liability:	
Per claim limit	1,000,000
Aggregate limit	1,000,000
Deductible	5,000

Underwriting

The company has a written underwriting guide. The guide covers all the lines of business that the company is presently writing.

The company has a formal inspection procedure for both new and renewal business. A sampling of new applications and renewal business is inspected by the President or the Treasurer of the company.

As part of the company's underwriting procedures, agents are required to submit photographs of all new and renewed policy risks. However, examiners' review of the company's policy files found that 15 out of 40 policy files reviewed didn't contain photographs (37.5%). Therefore, it is recommended that the company obtain photographs of all risks they are insuring and include them with their corresponding policy files in compliance with their underwriting procedures.

Claims Adjusting

The company has an adjusting committee consisting of at least three directors as required by s. 612.13 (4), Wis. Stat. The function of this committee is to adjust or supervise the adjustment of losses.

Accounts and Records

The examiners' review of the company's records indicated that the company is in compliance with s. Ins 13.05, Wis. Adm. Code, which sets forth the minimum standards for the handling of cash and recording of cash transactions by town mutual insurance companies. The examiners noted the following:

1. A proper policy register is maintained
2. A proper cash receipts journal is maintained
3. A proper cash disbursements journal is maintained
4. A proper general journal is maintained
5. A proper general ledger is maintained

It was noted while reviewing cash records that there were two large mispostings in the general ledger, including payments that were recorded twice to the same payee and an erroneous $16,686 adjustment to reconcile the bank statement balance at July 31, 2004, to what was reported on a system-generated cash disbursements report. The company's CPA properly made adjusting entries to correct these mispostings. However, there is no company procedure to correct differences between the company's disbursement reports, used to post in disbursements in the general ledger, to bank records. Therefore, it is recommended that the company reconcile the detailed reports, used to post onto the general ledger, on a monthly basis to provide for accurate internal records.

It was discovered per review of checks that cleared the bank, as part of cash disbursement testing, that 20 checks had check numbers listed on a system-generated report that were different from the check numbers listed in bank statements as been cleared. Discussion with company personnel found that check stock is pre-numbered, and when check printing errors occur the system will (unless the user takes an action) automatically print another check without making a correction to account for the new check number. Therefore, the check reported on the system will be one number off from what is actually printed on the check. In one instance this was the reason why the examination team was not able to find a missing check listed on the company's disbursement report. The system does allow the user to correct the problem when the printing error occurs. However, company personnel do not consistently perform the correction when this error occurs. Therefore, it is recommended that the company develop a control procedure to assure that the check numbers reported in its cash disbursement system are consistent with the checks actually printed and disbursed in compliance with s. Ins 13.05 (3) (c), Wis. Adm. Code.

An extensive review was made of income and disbursement items. Cash receipts were traced from source records and the proper recording and eventual deposit thereof ascertained. Negotiated checks issued during the period under examination were reviewed, test checked for proper endorsement, and traced to cash records. The verification of assets and determination of liabilities were made as of December 31, 2004.

The examination noted that the company's assistant manager performs the accounting function, reconciles bank accounts, and has check authorization. She also has access to open mail, handle cash receipts and complete deposit slips. It is a sound accounting control to segregate the duties of writing checks and handling of cash receipts from those performing accounting functions and reconciling month-end bank balances. Furthermore, the company has adequate staffing to better segregate the cash handling function. Therefore, it is recommended that the company properly segregate the duties of signing checks and handling of cash receipts from those of performing accounting functions and reconciling month-end bank balances in accordance with s. Ins 13.05 (4), Wis. Adm. Code.

The company is audited annually by an outside public accounting firm.

EDP Environment

Company personnel were interviewed with respect to the company's electronic data processing environment. Access to the computers is limited to people authorized to use the computers. Company personnel back up the computers daily and the backed-up data is kept off-site.

A manual which describes how to use the company's software and outlines the steps to complete specific tasks assists in the continuity of operations for seldom-used applications, training, or when staff turnover occurs. The company has manuals documenting the use of its software.

Business Continuity Plan

A business continuity plan identifies steps to be performed by a company in the event of business interruptions including, but not limited to, the inability to access its computer, the loss of information on its computer, the loss of a key employee, or the destruction of its office building. The company has developed a business continuity plan. The company's business continuity plan appears to be adequate.

Invested Assets

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

(1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and

(2) Any insurer may acquire and hold securities in bearer form.

For securities not held under a custodial agreement or trust arrangement with a bank or banking and trust company, s. Ins 13.05 (4), Wis. Adm. Code, requires that:

> Non-negotiable evidences of company investments such as registered bonds, certificates of deposits, notes, etc., shall be maintained in a safe or vault with adequate safety controls or in a safety deposit box in a bank. Negotiable evidences of company investments shall be maintained in a safety deposit box in a bank. Access to a company safety deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employees of the company.

The company is in compliance with these requirements.

Investment Rule Compliance

The investment rule for town mutual insurers allows a company to invest in common stocks, common stock mutual funds, and other higher risk investments (referred to as "Type 2") provided that the town mutual has a sufficient amount of lower risk investments (referred to as

"Type 1"). A town mutual may invest in Type 2 securities only if it already has sufficient Type 1 investments. Type 1 investments must equal or exceed the greater of items 1, 2, or 3.

1.	Liabilities plus $300,000	$1,577,508
2.	Liabilities plus 33% of gross premiums written	1,884,739
3.	Liabilities plus 50% of net premiums written	1,914,876
4.	Amount required (greater of 1, 2, or 3)	1,914,876
5.	Amount of Type 1 investments as of 12/31/2004	1,453,032
6.	Excess or (deficiency)	$ (461,844)

The company does not have sufficient Type 1 investments.

The company was granted an exception on July 20, 2000, by this office to hold up to 45% of admitted assets in common stocks, preferred stocks and convertible securities. There were no other investment exceptions granted.

Since the inception of the investment rule in 1996, the company has made additional Type 2 investments without having an adequate amount of Type 1 investments. This includes three separate stock issues that were acquired in 2000 and a cash deposit at interest with a cooperative in 2003. It is again recommended that the company make no additional Type 2 investments until the company meets the required amount of Type 1 investments, pursuant to s. Ins 6.20 (6) (c), Wis. Adm. Code. See the section titled "Other Invested Assets" for further information about the cash deposit with the cooperative noted above.

ASSETS

Cash and Invested Cash **$1,561,820**

The above asset is comprised of the following types of cash items:

Cash deposited in banks-checking accounts	$ 104,771
Cash deposited in banks at interest	1,457,049
Total	$1,561,820

Cash deposited in banks subject to the company's check and withdrawal consists of one account maintained in a local bank. Verification of checking account balance was made by obtaining a confirmation directly from the depository and reconciling the amounts shown thereon to company records.

Cash deposited in banks represents the aggregate of 24 deposits in 18 depositories. Deposits were verified by direct correspondence with the respective depositories and by an actual count and inspection of certificates and/or passbooks. Interest received during the year 2004 totaled $22,893 and was verified to company cash records. Rates of interest earned on cash deposits ranged from 1.45% to 3.3%. Accrued interest on cash deposits totaled $8,180 at year-end.

Stocks and Mutual Fund Investments **$536,608**

The above asset consists of the aggregate market value of stocks held by the company as of December 31, 2004. Stocks owned by the company are located in a vault at a financial institution.

Stock certificates were physically examined by the examiners. Stock purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in stocks was not in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. See the section titled “Investment Rule Compliance” for more details.

Dividends received during 2004 on stocks amounted to $14,694 and were traced to cash receipts records. Accrued dividends of $75 at December 31, 2004, were checked and allowed as a nonledger asset.

Book Value of Real Estate **$67,323**

The above amount represents the company's investment in real estate as of December 31, 2004. The company's real estate holdings consisted of the company's home office building.

The required documents supporting the validity of this asset were reviewed and were in order. Adequate hazard insurance was carried on the real estate and contents as noted under the caption, "Fidelity Bond and Other Insurance." The company's investment in real estate and related items was in conformance with the Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. Real estate depreciation is calculated using the straight-line method.

Other Invested Assets **$103,944**

The balance reported by the company as of December 31, 2004, represents an unsecured deposit with a cooperative that currently earns interest of 4%. The investment does not qualify as a Type 1 investment according to s. Ins 6.20 (6) (b), Wis. Adm. Code. As noted in the section titled "Investment Limitation Compliance" the company should not have invested in a Type 2 investment since they did not have sufficient Type 1 holdings. According to s. 612.36 (1) and (2), Wis. Stat., town mutual insurers are to make investments as if they were required to satisfy the compulsory surplus requirement of domestic insurers and therefore the company cannot simply retain and nonadmit this investment. It is recommended that the company withdraw their deposit with their cooperative within 60 days from the adoption of this examination report.

Premiums, Agents' Balances in Course of Collection **$51,827**

This original asset of $71,759 represents the amounts due from agents or policyholders which are not in excess of 90 days past due at year-end. A sample of detailed premium records was reviewed; examiners found two instances of policies that were canceled before year-end and three instances where the premiums were actually collected prior to year-end. It was also noted that the detail did not include $5.00 administrative fees charged two policyholders who made endorsements before year-end. According to Town Mutual Annual Statement Instructions, this balance is to include premiums and agents' balances due to the company, but which have not been collected. Since the examination team did not have the time to review the entire report for these reporting errors, examiners applied a ratio of total amount in error in the sample reviewed ($1,395) to the sample's original asset total reported in the premium detail ($5,022) and applied the 27.7% error rate to the premiums in course of collection balance reported on the annual statement. This resulted in an estimated adjustment of $19,932, which has been reflected in the section titled, "Reconciliation of Policyholders Surplus." It is therefore recommended that the company report premiums, agents' balances in course of collection in accordance with Town Mutual Annual Statement Instructions.

Premiums Deferred and Not Yet Due **$246,851**

This asset represents modal premium installments (such as monthly, quarterly, etc.) that are not yet due. A review of a sample from the company's detailed list of deferred premiums was utilized to test this asset. The above balance was decreased by $21,017 as a result of the reclassification described subsequently under the heading, "Premiums Received in Advance."

Investment Income Accrued **$8,255**

Interest due and accrued on the various assets of the company at December 31, 2004, consists of the following:

Cash Deposited at interest	$8,180
Stocks	75
Total	$8,255

To verify the above balance, the amounts were recalculated using outside source documentation as well as reviewing subsequent receipt of these amounts and tracing them to the cash receipts records.

Electronic Data Processing Equipment **$8,006**

The above balance consists of computer hardware and operating system software, net of depreciation as of December 31, 2004. A review of receipts and other documentation verified the balance. Nonoperating system software was properly nonadmitted.

Furniture and Fixtures **$0**

This asset consists of $1,735 of furniture and fixtures owned by the company at December 31, 2004. In accordance with annual statement requirements, this amount has been reported as nonadmitted asset, thus the balance shown above is $0.

LIABILITIES AND SURPLUS

Net Unpaid Losses **$113,500**

This liability represents losses incurred on or prior to December 31, 2004, that remained unpaid as of that date. The examiners reviewed the reasonableness of this liability by totaling actual loss payments made subsequent to December 31, 2004, with incurred dates in 2004 and prior years. To the actual paid loss figure was added an estimated amount for 2004 and prior losses remaining unpaid at the time of the examination. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule.

	Company Estimate	Examiners' Development	Difference
Incurred but unpaid losses	$212,842	$213,137	$ (295)
Less: Reinsurance recoverable on unpaid losses	99,342	80,035	19,307
Net Unpaid Losses	$113,500	$133,102	$(19,602)

The net difference is reflected in Section III of this report under the heading, "Reconciliation of Policyholders' Surplus."

The examiners' review of claim files included open claims, paid claims, claims closed without payment, and all claims which were denied during the examination period. The review indicated that claims are investigated and evaluated properly and that payments are made promptly and in accordance with policy provisions upon the submission of a proper proof of loss, except as described below. In addition, the review of claims handling procedures and files revealed the following:

1. A proper loss register is not maintained.
2. Claim files contained sufficient investigatory data and documentation to verify settlement payments or reserve estimates.
3. Proofs of loss were properly signed.

The examination noted that the company does not always assign claim numbers as soon as the claims are reported to them. Occasionally, the company assigns claim numbers when claims are either paid or settled. This procedure partially attributed to the company materially understating their net unpaid loss liability by at year-end. According to s. Ins 13.05 (4) (e), Wis. Adm. Code, all claims reported to the company shall be assigned a claim number when reported. Therefore it is recommended that the company assign a claim number to claims as soon as they are reported in accordance with s. Ins 13.05 (4) (e), Wis. Adm. Code.

The examination also noted that the company routinely allows claims to remain open for a number of years without settlement while the company waits for information from the claimant or for the insured to repair covered damages. This practice may be interpreted to be an unfair settlement policy by failure to initiate and conclude claim investigations in a reasonable period of time. It also increases the company's exposure to additional loss sustained on damaged and unrepaired property. It was also noted that the company had a number of older claims open at year-end 2004 that should have been closed due to various reasons. It is recommended that the company adopt procedures for timely settlement and closing of claims in compliance with s. Ins 6.11 (3) (a) 2, Wis. Adm. Code.

Unpaid Loss Adjustment Expenses $700

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2004, but which remained unpaid as of year-end. This liability is established with the assistance of the company's auditors who adjust the unpaid LAE balance reported in the previous year to reflect the increase in unpaid losses in the current year.

The examiners' analysis of expenses incurred in the current year related to the settlement of prior year losses, as well as estimates of amounts necessary to settle any prior losses remaining unpaid at the examination date, determined this liability to be adequately stated.

Commissions Payable $43,700

This liability represents the commissions payable to agents as of December 31, 2004. The examiners reviewed the company's commission calculation and found the liability to be reasonably stated.

Fire Department Dues Payable $2,170

This liability represents the fire department dues payable to the State of Wisconsin as of December 31, 2004. The examiners reviewed the company's fire department dues calculation and found this liability to be correctly calculated. The actual amount paid was verified to the cash disbursement records.

Federal Income Taxes Payable **$112,334**

This liability represents the balance payable at year-end for federal income taxes incurred prior to December 31, 2004. The examiners reviewed the company's 2004 tax return and verified amounts paid to cash disbursement records to verify the accuracy of this liability.

Unearned Premiums **$874,693**

This liability represents the reserve established for unearned premiums in compliance with s. Ins 13.08 (3), Wis. Adm. Code. This reserve was established using a daily pro rata methodology.

Reinsurance Payable **$70,656**

This liability consists of amounts due to the company's reinsurer at December 31, 2004, relating to transactions which occurred on or prior to that date. Amounts listed below reflect the year-end adjustments for the company’s written premium results and the reinsurer’s portion of deferred premiums at year-end.

Contract Description	Amount
Class A, Liability	$32,506
Class C-1, Excess of Loss	6,700
Class C-2, Excess of Loss	3,100
Class D/E, Stop Loss	9,100
Deferred Reinsurance Premium Payable	19,250
Total	$70,656

Subsequent cash disbursements and reinsurance accountings verified the amount of this liability.

Amounts Withheld for the Account of Others **$5,234**

This liability represents employee payroll deductions in the possession of the company at December 31, 2004. Supporting records and subsequent cash disbursements verified this item.

Payroll Taxes Payable **$1,090**

This liability represents the company's portion of payroll taxes incurred prior to December 31, 2004, which had not yet been paid. Supporting records and subsequent cash disbursements verified this item.

Accounts Payable **$1,221**

This liability represents amounts for expenses incurred in 2004 but not paid as of year-end. A search for unrecorded liabilities as well as review of subsequent cash disbursements verified this balance.

Accrued Property Taxes **$3,691**

This liability represents the amount of 2004 property taxes that are unpaid as of December 31, 2004. The balance includes taxes on both real property and personal property. The accrued amount was traced to 2004 property tax documents and a subsequent payment to verify the balance.

Premiums Received in Advance **$27,502**

This liability represents the total premiums received prior to year-end for policies with effective dates after December 31, 2004. The company reported a year-end advance premiums balance of $48,519. Examiners tested the company's year-end advance premium detail and found that it included premiums received in advance of the effective date of the policy as well as premiums received in advance of the modal/installment due date of the policy. According to the <u>Town Mutual Annual Statement Instructions</u> the balance should only include premiums received in advance of the effective of the policy. The calculated adjustment for this finding was a $21,017 decrease to Premiums Deferred and Not Yet Due and is reflected in Section III of this report under the heading, "Examination Reclassifications." It is recommended that the company report advance premiums in accordance with the <u>Town Mutual Annual Statement Instructions</u>.

V. CONCLUSION

The examination of the Medina Mutual Insurance Company resulted in ten recommendations, one of which was repeated from the prior examination, one reclassification and two adjustments to policyholder's surplus reducing it by $39,534. The recommendations relate to a variety of different topics including proper segregation of duties, having adequate control over basic accounting functions, and making purchases of Type 1 investments when the company was not in compliance with the investment rule. The comments and recommendations are summarized in the subsequent section. The adjustments and reclassification were made to correct reporting errors for two premium account balances as well as deficiencies in the year-end unpaid loss reserve balance.

The company's surplus per examination of $1,308,541 represents a 26% increase over the past five years. The company experienced underwriting gains four of the past five years. The company's net loss and LAE ratio for the past five years averaged 52% and its expense ratio averaged 41%. Surplus increased primarily due to the significant increase in premium written coupled with favorable weather conditions. On a gross basis, premium writings have increased by 204% partially due to rate increases, inflation in housing prices, but mostly due to an aggressive marketing strategy. The company plans on continuing this trend in the future.

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 15 - Underwriting—It is recommended that the company obtain photographs of all risks they are insuring and include them with their corresponding policy files in compliance with their underwriting procedures.

2. Page 16 - Accounts and Records—It is recommended that the company reconcile the detailed reports, used to post onto the general ledger, on a monthly basis to provide for accurate internal records.

3. Page 17 - Accounts and Records—It is recommended that the company develop a control procedure to assure that the check numbers reported in its cash disbursement system are consistent with the checks actually printed and disbursed in compliance with s. Ins 13.05 (3) (c), Wis. Adm. Code.

4. Page 17 - Accounts and Records—It is recommended that the company properly segregate the duties of signing checks and handling of cash receipts from those of performing accounting functions and reconciling month-end bank balances in accordance with s. Ins 13.05 (4), Wis. Adm. Code.

5. Page 19 - Investment Rule Compliance—It is again recommended that the company make no additional Type 2 investments until the company meets the required amount of Type 1 investments, pursuant to s. Ins 6.20 (6) (c), Wis. Adm. Code. See the section titled "Other Invested Assets" for further information about the cash deposit with the cooperative noted above.

6. Page 21 - Other Invested Assets—It is recommended that the company withdraw their deposit with their cooperative within 60 days from the adoption of this examination report.

7. Page 22 - Premiums in Course of Collection—It is therefore recommended that the company report premiums, agents' balances in course of collection in accordance with Town Mutual Annual Statement Instructions.

8. Page 25 - Net Unpaid Losses—It is recommended that the company assign a claim number to claims as soon as they are reported in accordance with s. Ins 13.05 (4) (e), Wis. Adm. Code.

9. Page 25 - Net Unpaid Losses—It is recommended that the company adopt procedures for timely settlement and closing of claims in compliance with s. Ins 6.11 (3) (a) 2, Wis. Adm. Code.

10. Page 27 - Premiums Received in Advance—It is recommended that the company report advance premiums in accordance with the Town Mutual Annual Statement Instructions.

VII. ACKNOWLEDGMENT

The courteous cooperation extended to the examiners by the company's personnel is hereby acknowledged.

In addition to the undersigned, Angelita Romaker of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination.

Respectfully submitted,

John Litweiler
Examiner-in-Charge